



## Legislative Bulletin.....April 9, 2002

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- **H. R. 3991**—Taxpayer Protection and IRS Accountability Act of 2002

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### **H. R. 3991—Taxpayer Protection and IRS Accountability Act (Houghton)**

**Order of Business:** The bill is scheduled to be considered on Tuesday, April 9, under a motion to suspend the rules and pass the bill.

### Summary:

#### **KEY PROVISIONS**

- **First Time Penalty Waiver** -- The reasonable cause standard, as applied to failure to file and failure-to-pay penalty abatement, would be expanded to include situations where the taxpayer's minor negligence results in the imposition of a penalty that is disproportionate to the underlying error. Relief would be where abatement of the penalty would promote voluntary compliance and effective tax administration. Eligibility for relief would be determined with reference to the taxpayer's prior history of tax compliance. The provision would apply to individual income tax liabilities only.
- **Violations Resulting in Dismissal of IRS Employees** -- Make unauthorized browsing of taxpayer records one of the "ten deadly sins" for IRS Employees and grant the IRS Commissioner authority to specify penalties up to and including termination for improper activities by IRS employees. Remove the termination provision for the late filing of a return by an IRS employee in cases where the employee has no Federal income tax liability. It would limit the ability of IRS employees to file complaints against managers or other employees under the Internal Revenue Service Restructuring Act.
- **Extend Due Date for Electronically Filed Returns** -- Extend the return filing and payment deadline for the filing of individual income tax returns from April 15 to April 30, if the return is filed electronically.
- **Clarification of Church Tax Inquiry** -- Clarify that the IRS would not violate the church-tax-inquiry procedures when written materials are provided to a church for the purpose of educating the church with respect to the law, for example the types of activities that are not permissible under section 501(c)(3).

### **Revisions to 527 Organization Reporting Requirements:**

- Eliminate the requirement that political committees of state or local candidates or parties register with the IRS as 527 organizations.
- Exempt from the reporting requirements all State or local 527 organizations if they only engage in state or local political activity AND they are subject to substantially similar state or local reporting on their expenditures and contributions. State or local committees directed by federal candidates or officeholders would still be required to file the federal report.
- Eliminate the requirement that party committees and federal and state candidate committees file Form 990 informational tax returns.

### **ADDITIONAL PROVISIONS**

#### **Penalty and Interest Provisions:**

- **Repeal Estimated Tax Penalty: Convert to Interest & Simplify Estimated Tax Calculation** -- Converts the present-law penalty for failure to pay estimated tax into an interest provision, increases the threshold for underpayment of estimated tax from \$1,000 to \$2,000, and allows both tax withheld and estimated tax paid equally throughout the year to be considered in determining whether the threshold has been met.
- **Exclude Interest on Overpayments from Gross Income** -- Exclude from gross income interest that is paid by the IRS to individual taxpayers on overpayments of Federal income tax.
- **Abatement of Interest Attributable to Reliance on IRS Written Statements and With Respect to Erroneous Refunds** -- Allow the IRS to abate interest to the extent such interest is attributable to taxpayer reliance on IRS written advice. Additionally, allow abatement of interest from erroneous refunds until the date of the IRS's demand for payment, without regard to the size of the refund, unless the taxpayer caused the erroneous refund or has actual notice of the erroneous refund and does not promptly notify the IRS.
- **Allow Taxpayers to Limit Underpayment Interest Through Use of a Qualified Reserve Account** -- Allow taxpayers to limit their exposure to underpayment interest through the use of a qualified reserve account. Amounts deposited in a qualified reserve account could either be withdrawn with interest or used to offset an underpayment of tax. The use of a qualified reserve account would not affect the ability of the taxpayer to be heard by the Tax Court.
- **Expand Interest Netting for Individuals** -- Apply the interest netting rules without regard to the 45-day period in which the Secretary may refund an overpayment of tax without the payment of interest. Solely for the purpose of applying the interest netting rules, individual taxpayers may treat such period as a period for which interest is allowable on an overpayment at a zero percent rate.
- **Frivolous Filer Penalty** -- Allow the imposition of penalties for submitting any document that contains frivolous arguments and to allow summary dismissal of frivolous submissions without further review. Currently, the frivolous filer penalty may be imposed only in connection with the filing of a frivolous Federal income tax return. Submissions containing frivolous and non-frivolous arguments would continue

to be reviewed. In addition, the maximum penalty for filing a frivolous document would be increased from \$500 to \$5,000. In addition, the Secretary would be required to publish a list of what are considered frivolous submissions.

- **Reduce Federal Tax Deposit (FTD) Avoidance Penalty** -- Reduce from 10% penalty to 2% the penalty for failure to make a federal tax deposit in the manner prescribed.

#### **IRS Collection Procedures:**

- **Allow Partial Pay Installment Agreements** -- Allow taxpayers to enter into installment agreements that do not fully satisfy their tax obligations. The IRS would be required to re-evaluate the taxpayer's ability to pay at least once every two years during the running of the ten-year statute of limitations on collections. Current law only allows the IRS to enter into an agreement to either collect 100% of the tax obligation or nothing.
- **Extend Time Limit for Contesting IRS Levy and Allow IRS to Restore Retirement Accounts** -- Extend the time limit for contesting an IRS levy, generally, from 9 months to 2 years, and to 4 years in cases where the levy was in reckless disregard of established IRS rules and procedures. Allow wrongfully levied funds to be returned to retirement accounts with interest paid to make the taxpayer whole.
- **Place Threshold on Tolling of Statute of Limitations During Taxpayer Advocate Service Review** -- Impose a 7-day threshold on suspensions of the statute of limitations during Taxpayer Advocate Service review. The statute of limitations on collections would be suspended only in cases where the Taxpayer Advocate Service review lasts more than 7 days.
- **Study of IRS Liens and Levies** -- The IRS would be required to study and report to Congress on tax liens and levies.

#### **Tax Administration:**

- **Grant Tax Court Equitable Recoupment Jurisdiction** -- Expand the Tax Court's jurisdiction to allow the Tax Court to apply the doctrine of equitable recoupment to the same extent as is currently allowed in district court and the Court of Federal Claims.
- **Consolidate in Tax Court Review of Collection Due Process Cases** -- Make the United States Tax Court the exclusive venue for a taxpayer to obtain judicial review of any Notice of Determination issued by an IRS Appeals Office in a Collection Due Process (CDP) hearing. Currently, the venue for CDP hearings is determined by the venue for the underlying tax liability. For example, CDP hearings arising out of employment and excise tax collection activities may currently only be heard in U.S. District Courts.
- **Remove Monetary Threshold for Counsel Review of OIC Proposals** -- Eliminate the requirement that the IRS Chief Counsel provide an opinion for any accepted offer-in-compromise of \$50,000 or more. The proposal would require the Secretary to establish standards for determining when Chief Counsel review is appropriate.

#### **Taxpayer Information Confidentiality:**

- **Disclosure of Collection Activity on Oral Request** -- Eliminate the requirement for

former spouses to make a written request for disclosure of collection activities with respect to a joint return.

- **Limit Inspection of Return Preparers** -- IRS employee conducting an examination of a taxpayer is not authorized to inspect a taxpayer representative's return or return information solely on the basis of the representative relationship to the taxpayer. Under the proposal, the supervisor of the IRS employee would have to approve such inspection after making a determination that other grounds justified such an inspection.
- **Limit Non-Party Return Information Disclosure** --Require that only the portions of a nonparty return or return information that directly relate to the resolution of an issue in the proceeding would be disclosed in such proceeding. The nonparty would be given reasonable notice prior to the disclosure and the opportunity to request that certain material be deleted from the information to be disclosed.
- **Offers-in-Compromise Related Disclosure** -- Prohibit the disclosure of the taxpayer's address and taxpayer identification number as part of the publicly available summaries of accepted offers in compromise.
- **State Contractor Confidentiality Safeguards** -- Require that a State conduct annual on-site reviews of all of its contractors receiving Federal returns and return information as agents of the State tax administration agency. The reviews would assess the contractors' efforts to safeguard Federal returns and return information. The State would be required to submit a report of its findings to the IRS and certify annually that all contractors are in compliance with the requirements to safeguard the confidentiality of Federal returns and return information.
- **Dating of Disclosure Consent Forms** -- Render invalid a consent that does not designate a recipient or is not dated at the time of execution. The person submitting the consent to the IRS would be required to verify under penalties of perjury that the form was complete and dated at the time it was signed by the taxpayer. The proposal would require the consent form to contain a warning, prominently displayed, informing the taxpayer that he or she should not sign the form unless it is complete and dated. The proposal would require the consent form to state that the taxpayer should report any attempts to coerce the signing of an incomplete form to the Treasury Inspector General for Tax Administration. The telephone number for the Treasury Inspector General for Tax Administration would be included on the form. All third parties receiving returns and return information by consent would be required to: (1) ensure that the information received will be kept confidential; (2) use the information only for the purpose for which it was requested; and (3) not further disclose the information except to accomplish that purpose, unless a separate consent from the taxpayer is obtained. The Treasury Inspector General for Tax Administration would be required to investigate a random sampling of consents and report on the effectiveness of the provision eighteen months after the date of enactment.
- **Notice to Taxpayer of Return Browsing** -- The IRS would be required to notify a taxpayer after the Treasury Inspector General for Tax Administration determines that a taxpayer's return or return information has been disclosed or inspected without authorization. The IRS would be required to provide information on unauthorized disclosures or inspections of return and return information in its public annual report to the Joint Committee on Taxation.

- **Expand Disclosure in Emergency Circumstances --** In cases where a taxpayer threatens suicide as part of a tax-related communication, the proposal would allow the IRS to contact local law enforcement agencies and to disclose relevant return information.
- **Disclosure of Identity for Tax Refund Purposes --** Allows the IRS to notify taxpayers of unclaimed refunds through the Internet.
- **Increase Tax-Exempt Organization Disclosure to State Charity Officials --** Expands the disclosure to State Attorneys General to enable them to better administer State laws regulating charities.

#### **Miscellaneous:**

- **Extension of Declaratory Judgment Procedures --**Extends declaratory judgment procedures similar to those currently available only to charities under section 7428 to other section 501(c) determinations.
- **Treasury Inspector General for Tax Administration Report on Employee Misconduct --** Modify the present-law requirement that the Treasury Inspector General for Tax Administration include a summary of allegations of employee misconduct in its semi-annual report. Under the proposal, the Treasury Inspector General for Tax Administration, in its semi-annual report, would be required to include a description of the ten most common complaints of employee misconduct and the number of complaints made in each such category.
- **Annual Report on Attorney's Fees --**Direct the Treasury Inspector General for Tax Administration to submit to Congress annually a report on awards of costs and certain fees (such as attorney's fees) in administrative and court proceedings. The report would include an analysis of administrative issues giving rise to such payments and changes that would be made as a result of such analysis.
- **Annual Report on Abatement of Penalties --** Direct the Treasury Inspector General for Tax Administration to submit to Congress annually a report on abatements of penalties under the Internal Revenue Code.
- **Report on E-Mail/Fax Communication with Taxpayers --** Require the Treasury Inspector General for Tax Administration to submit to Congress no later than 18 months after the date of enactment a report evaluating whether technological advances, such as e-mail and facsimile transmission, permit the use of alternative means for the IRS to communicate with taxpayers.
- **Form 1040 Statute of Limitations Disclosure --**Require the IRS to revise Publication 1 (Your Rights as a Taxpayer) and the instructions for Form 1040 packages to add a description of the statute of limitations and an explanation of the consequences of failing to file within the prescribed time period.
- **Treasury Bond Advisory Council Amendments --** Amend restrictions on trading by Advisory Council members to allow trading after publication of official meeting minutes.
- **Enrolled Agent Designation --** Codify the authority of the Secretary to issue regulations covering the practices of enrolled agents before the IRS.
- **Allow Financial Management Services (FMS) to Retain Service Fee --** Allow the Financial Management Service (FMS) to retain directly a portion of funds levied from delinquent taxpayers as a payment for FMS's services. The taxpayer would receive

full credit for the levied amount; the FMS fee would in no way increase the taxpayer's costs.

- **Capital Gains Treatment to Apply to Outright Sales by Land Owner --** Allows land owners to enter into contracts to sell timber without retaining an economic interest in the timber and still qualify for capital gains treatment, pursuant to IRC Section 631(b).

#### **Changes in Appropriations Set-Asides and Other Changes:**

- **Low Income Taxpayer Clinics (LITC)--** Increase the existing \$6 million set-aside cap for the LITC program to the following amounts in the coming years: 2002: \$9 million; 2003: \$12 million; and 2004 and succeeding years: \$15 million.
- Clarify existing law to provide that Low Income Taxpayer Clinics may qualify for federal funds by virtue of their service to individuals for whom English is a second language, but only if the programs operated by such clinics do not include routine tax preparation.
- Allow National Taxpayer Advocate to refer taxpayers to Low Income Taxpayer Clinics for assistance.

**Cost to Taxpayers:** The Joint Tax Committee estimated that the revenue portions of the Chairman's mark would increase revenue by \$1.014 billion in FY '03 (primarily as a result of the provision that excludes from gross income interest on overpayments of income tax by individuals). Over the period 2002-2007 the Chairman's mark would increase revenue by \$156 million, and over the period 2002-2012, the Chairman's mark would reduce revenue by \$1.2 billion. **NOTE:** It is expected that some slight changes will be made before floor consideration that will result in a smaller reduction in revenue.

**Does the Bill Create New Federal Programs or Rules?:** The bill modifies existing IRS rules and regulations as set out above. The bill does not create any new programs.

**Constitutional Authority:** A Committee Report citing Constitutional Authority is unavailable.

**Talking Points:** One of the key provisions of the bill is the provision to allow the IRS to waive penalties for first time violations resulting from minor, unintentional negligence. The following examples may help with floor debate or press releases:

Example (1) An individual uses an accountant to file his return that has a balance due. He has filed consistently, on time, for the past ten years, and, overall, he has a good record of compliance. He signs the return and provides all information requested by the accountant on time, but the accountant loses the return. Two months later, the taxpayer receives a late notice from the IRS and he investigates. He files a spare copy of the return the next day. The provision would allow the IRS Commissioner to waive the Failure to File and Failure to Pay penalties.

Example (2) Same facts as above except that instead of using an accountant, the taxpayer files himself using the office postage meter. He personally checks that the date on the metered

envelope says "April 14th," before mailing his return, but the return is lost in the mail and it arrives two weeks late. The Failure to File and Failure to Pay penalties are assessed, because, unknown to the taxpayer, only a U.S. Postal Service date stamp can establish the date of mailing. Even though the IRS can see that his return is stamped April 14th, the IRS will not accept this private stamp as proof of mailing unless the taxpayer can show why the mail was delayed. The provision in the Bill would encourage the IRS Commissioner to waive the 5% Failure to File and the 0.5% Failure to Pay penalties in this and similar cases.

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